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DEPARTMENT OF AUDITOR-CONTROLLER**

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April 8, 2009

TO: Supervisor Don Knabe, Chairman  
Supervisor Gloria Molina  
Supervisor Mark Ridley-Thomas  
Supervisor Zev Yaroslavsky  
Supervisor Michael D. Antonovich

FROM:

Wendy L. Watanabe  
Auditor-Controller

SUBJECT: **FISCAL REVIEW OF PSYMED, INCORPORATED (dba HUDSON  
LYNDSEY GROUP HOME) - A GROUP HOME FOSTER CARE  
CONTRACTOR**

Attached is our report on the fiscal operations of PsyMed, Incorporated, also doing business as Hudson Lyndsey Group Home (Hudson or Agency), from January 1, through December 31, 2006. Hudson is licensed to operate three group homes (GH), each with a resident capacity of six children. Two of the Agency's group homes are located in the Second Supervisorial District and the third home is located in Orange County.

The Department of Children and Family Services (DCFS) and the Probation Department (Probation) contract with Hudson to care for foster children placed in the Agency's homes. Under the contract, the County pays Hudson \$4,479 a month per child, based on a rate determined by the California Department of Social Services. During Calendar year 2006, the Agency received \$682,681 in GH foster care funds.

Hudson has closed its group homes. DCFS informed us that all children placed by Los Angeles County were removed from Hudson on February 6, 2008 and the Agency was placed on Do Not Use status, effective April 4, 2008.

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### **Scope**

The purpose of our review was to determine whether Hudson complied with its contract terms and appropriately accounted for and spent foster care funds on allowable and reasonable expenditures. We also evaluated Hudson's expenditure and revenue documentation, internal controls and compliance with applicable federal, State and County fiscal guidelines for GH foster care funds.

### **Summary of Findings**

We identified \$2,741 in unallowable costs and \$172,179 in unsupported/inadequately supported costs. In addition, DCFS needs to resolve some potential overpayments.

More significantly, we noted that Hudson has not maintained the financial records required by the contract, such as a double-entry accounting system and a General Ledger. As a result, we could not determine if the Agency has any net assets. Agency management advised us that the most recent Single Audit of Hudson was for the calendar year ended December 2001. However, the Agency could not provide a copy of the audit report and DCFS advised us that Hudson did not file a copy of their Single Audit for this period, or any subsequent periods. According to the California Department of Social Services (CDSS), the Agency has not submitted the required Group Home Program Cost Report (SR-3) and Group Home Program Payroll and Fringe Benefit Report (SR-4), and has not submitted contractually required Semi-Annual Expenditure Reports to DCFS.

CDSS advised us that on December 2, 2007, the Foster Care Rates Bureau issued a Rate Determination Letter and informed Hudson that it would be terminating the Agency's program rate effective March 1, 2008, because no rate application was submitted. DCFS also advised us that the Community Care Licensing Division was in the process of revoking the facility licenses for Hudson's group homes for failure to submit a facility package and failure to pay the renewal fees on these properties. As previously indicated, all children were removed from the Agency on February 6, 2008 and Hudson was placed on Do Not Use status effective April 4, 2008. Hudson subsequently closed its group home operations.

Our review also disclosed other contract non-compliance and internal control deficiencies. Specifically, Hudson needs to strengthen its internal controls over accounting and disbursements, payroll/personnel procedures, establish independent contractor agreements, deposit funds timely, perform monthly bank reconciliations and document its board of directors' meetings. Details of our findings are discussed in the attached report.

We have recommended that DCFS resolve the questioned costs and collect any disallowed amounts. If DCFS contracts with Hudson in the future, DCFS needs to ensure that Hudson's management takes action to address the recommendations in this report and monitor to ensure that the actions result in permanent changes.

### **Review of Report**

Hudson's management declined to meet with us to review this report and has closed its group home operations. DCFS needs to work with Hudson to resolve the findings noted in our report.

Please call me if you have any questions, or your staff may contact Jim Schneiderman at (213) 253-0101.

WLW:MMO:JLS:MWM

Attachment

c: William T Fujioka, Chief Executive Officer  
Patricia S. Ploehn, Director, Department of Children and Family Services  
Ted Myers, Chief Deputy Director, Department of Children and Family Services  
Susan Kerr, Senior Deputy Director, Department of Children and Family Services  
Robert B. Taylor, Chief Probation Officer  
Diana Mitchell, Executive Director, Hudson Lyndsey Group Home  
Board of Directors, Hudson Lyndsey Group Home  
California Department of Social Services  
Cora Dixon, Bureau Chief, Foster Care Audits Bureau, CA Dept. of Social Services  
Commission for Children and Families  
Public Information Office  
Audit Committee

**Hudson Lyndsey Group Home (aka PsyMed, Incorporated)**  
**Fiscal Review**

**REVIEW OF EXPENDITURES/REVENUES**

We identified \$2,741 in unallowable costs and \$172,179 in unsupported/inadequately supported costs. In addition, DCFS and the Agency need to work together to resolve potential overpayments. Details of these costs/overpayments are discussed below.

**Applicable Regulations and Guidelines**

Hudson was required to operate its GH in accordance with the following federal, State and County regulations and guidelines:

- GH Contract, including Exhibit C-1, Auditor-Controller Contract Accounting and Administration Handbook (A-C Handbook)
- Federal Office of Management and Budget Circular A-122, Cost Principles for Non-Profit Organizations (Circular)
- California Department of Social Services Manual of Policies and Procedures (CDSS-MPP)
- California Code of Regulations, Title 22 (Title 22)

**Unallowable Costs**

We identified \$2,741 in fines and penalties, consisting of non-sufficient fund (NSF) and overdraft fees charged by the Agency's bank. Fines and penalties are unallowable costs according to Circular Section 16.

**Unsupported/Inadequately Supported Costs**

A-C Handbook Section A.3.2 states that all expenditures shall be supported by original vouchers, invoices, receipts, or other supporting documents, and that unsupported expenditures will be disallowed upon audit. Photocopied invoices or receipts, any internally generated documents (i.e., vouchers, request for check forms, requisitions, cancelled checks, etc.), and account statements do not constitute supporting documentation for purchases

We identified \$172,179 in expenditures that were unsupported or inadequately supported.

- \$63,595 in unsupported costs involving ATM cash withdrawals and checks payable to cash. The Agency did not provide receipts, invoices or any other documentation to support these expenses. Therefore, we could not determine whether these expenses benefited the group home program.
- \$108,584 in inadequately supported costs involving utilities, auto expenses, insurance, payments to the Executive Director, payments to a board member, a tree service business, a financing company, cable television, casinos/hotels, airline tickets, clothing stores, car rentals, the State of Nevada, restaurants, beauty supplies, a home lending company and independent contractors. Hudson provided cancelled checks and identified the payees. However, the Agency did not provide receipts, invoices, written contractor agreements, or other supporting documentation indicating how the expenses benefitted the group home program.

**Recommendations**

1. DCFS management resolve the \$174,920 (\$2,741 + \$172,179) in questioned costs and collect any disallowed amounts.

If DCFS considers contracting with Hudson in the future, Hudson management:

2. Ensure that foster care funds are used for allowable expenditures to carry out the purpose and activities of the Agency.
3. Maintain adequate supporting documentation for all Agency expenditures, including original itemized receipts and invoices.

**Potential DCFS Overpayments**

DCFS' records show some overpayments made to the Agency. DCFS and the Agency should work together to resolve the overpayments and DCFS should collect any verified overpayments. Hudson management should ensure that any future payment discrepancies are immediately reported to DCFS and any excess amounts are repaid promptly.

**Recommendations**

4. DCFS management work with Hudson to resolve the overpayments and collect any verified overpayments.
5. If DCFS considers contracting with Hudson in the future, Hudson management ensure that any future payment discrepancies are

**immediately reported to DCFS and any excess amounts are repaid promptly.**

### **CONTRACT COMPLIANCE AND INTERNAL CONTROLS**

We noted serious contract non-compliance issues and internal control weaknesses that we believe contributed to the questioned costs identified above. If DCFS considers contracting with Hudson in the future, DCFS must ensure that Hudson's management takes action to address each of the recommendations in this report. DCFS must also monitor to ensure the actions result in permanent changes.

### **Financial Records**

A-C Handbook Section A.2.0 requires group home contractors to maintain a double entry accounting system, general journal, cash receipts journal, general ledger and cash disbursements journal. Hudson did not maintain the required accounting records. The Agency only had the bank statements, check register, cancelled checks, personnel files, employee time sheets, etc.

In addition, DCFS Contract Section 11.8 requires agencies to have annual or triennial financial audits. OMB Circular 133 and A-C Handbook Section A.6.0 requires organizations who receive federal funds, including pass-through awards, to have Single Audits, and file a copy of the Single Audit report with the County.

Hudson management indicated that the most recent Single Audit that included the Group Home program was for the year ended December 31, 2001. However, the Agency was unable to provide a copy of the audit report and DCFS advised us that they did not receive a copy of the audit for 2001 or any subsequent periods. However, the California Department of Social Services (CDSS) advised us that Hudson had filed a Single Audit for the calendar year ended December 31, 2002.

In addition, the Agency had not submitted the required Group Home Program Cost Report (SR-3) and Group Home Program Payroll and Fringe Benefit Report (SR-4) to CDSS, nor had it submitted the contractually required Semi-Annual Expenditure reports to DCFS.

If DCFS considers contracting with Hudson in the future, the Agency should submit a plan to immediately begin maintaining all financial records required by the A-C Handbook, develop prior financial records and submit all delinquent Semi-Annual Expenditure reports to DCFS. In addition, the Agency will need to work with CDSS to develop a plan to provide delinquent Single Audits and SR-3 and SR-4 reports.

Because the Agency did not have audited financial statements and did not maintain financial records, such as a general ledger, we could not determine if the Agency has any net assets. Hudson cannot use current period foster care funds to pay for any

delinquent Single Audits or to develop prior period financial records. If DCFS considers contracting with Hudson in the future, the Agency should submit a plan to DCFS demonstrating how these tasks will be accomplished without using current period foster care funds.

**Recommendations**

**If DCFS considers contracting with Hudson in the future, Hudson management:**

- 6. Submit a plan to immediately begin maintaining all financial records required by the A-C Handbook and develop any required financial records that were not maintained in prior contract periods.**
- 7. Work with CDSS to develop a plan to provide delinquent audited financial statements and SR-3 and SR-4 reports.**
- 8. Complete and submit all delinquent Semi-Annual Expenditure reports.**
- 9. Submit a plan to DCFS demonstrating how the Agency will complete the delinquent Single Audits and reconstruct its prior financial records without using current period GH funds.**
- 10. DCFS management closely monitor Hudson's implementation of its plan to develop non-current financial records and maintain all required financial records.**

**Fixed Asset List**

We noted that the Agency did not maintain a fixed assets list during our review period. A-C Handbook Section B.4.2 requires each agency to maintain a current list of fixed assets, including the item description, serial number, date of purchase, acquisition cost and source of funding.

**Recommendation**

- 11. If DCFS considers contracting with Hudson in the future, Hudson management maintain a list of fixed assets as required by the A-C Handbook.**

**Board Minutes**

California Corporations Code Section 6320 requires nonprofit corporations to keep a written record of their board of directors meetings. Hudson did not provide board

minutes for our review. Hudson management needs to comply with the California Corporations Code in documenting the actions taken for each of their board meetings.

**Recommendation**

- 12. If DCFS considers contracting with Hudson in the future, Hudson management comply with the California Corporations Code by keeping written records of each board of directors' meeting.**

**Disbursement Procedures**

We noted weaknesses in the Agency's disbursement procedures, as follows:

- Fifteen of 48 checks reviewed (31%), totaling \$42,208, were made payable to cash. A-C Handbook Section B.2.1 states that checks should not be payable to cash.
- Six of 48 checks reviewed (13%), totaling \$3,304, were payable to the Executive Director, who also signed the checks. On checks where the signer is also the payee, a second signature by someone independent of the payee (such as a Board member), should be required to verify the appropriateness of the expense. A-C Handbook Section B.2.2 requires a second signature on all checks.

**Recommendations**

**If DCFS considers contracting with Hudson in the future, Hudson management:**

- 13. Ensure that checks are not made payable to cash.**
- 14. Require two signatures on all checks where the payee and the check signer are the same.**

**Payroll/Personnel Controls**

CDSS MPP Section 11-402 requires that supporting documentation be maintained for all program expenditures, including employee salary rates. In addition, A-C Handbook Section B.3.1 states that timecards or time reports must be prepared for each pay period, and all timecards or time reports must be signed in ink by the employee and the employee's supervisor to certify the accuracy of the reported time.

We sampled the personnel files and payroll records of 12 Agency employees and noted the following:

- Ten personnel files (83%) did not contain a current salary/pay rate sheet.



- Total hours on one employee time sheet (8%) did not match the hours on the payroll register. The employee was underpaid eight hours.
- The Executive Director signed and approved his own timecard. We recommend someone else such as a board member approve the Executive Director's timecard.

**Recommendations**

**If DCFS considers contracting with Hudson in the future, Hudson management:**

- 15. Ensure employee salary/pay rates are consistently documented and updated in the employees' personnel files.**
- 16. Ensure time sheet hours match the payroll register and properly pay the employee that was underpaid.**
- 17. Ensure timecards are approved by someone other than the employee.**

**Independent Contractors**

A-C Handbook Section A.3.2 requires an agency to have a contract, time and attendance records, billing rates and other supporting documentation for contract services. Our review of five independent contractors hired by the Agency disclosed the following:

- The Agency had no written agreements with four of the five independent contractors.
- The Agency did not provide 1099s for the contractors we reviewed. Therefore, we do not know if the Agency issued any 1099s to its contractors for calendar year 2006.

**Recommendations**

**If DCFS considers contracting with Hudson in the future, Hudson management:**

- 18. Establish written agreements with contractors that indicate the billing rates and services to be provided by the contractors.**
- 19. Ensure that 1099s are issued to all independent contractors.**

**Untimely Deposits**

A-C Handbook Section B.1.2 states that cash receipts totaling \$500 or more should be deposited within one day of receipt. Hudson did not deposit their foster care funds timely. Thirty-two of the 164 County warrants, totaling \$106,393, were cashed/deposited seven or more days after the warrants' issue date. Two warrants were deposited as long as 27 days after the issue date. Hudson needs to ensure that it deposits County payments timely. The Agency should consider having their County payments deposited directly into their bank account.

**Recommendation**

20. If DCFS considers contracting with Hudson in the future, Hudson management ensure that Los Angeles County warrants are deposited timely and consider having its County payments deposited directly into the Agency bank account.

**Bank Reconciliations**

A-C Handbook Section 1.4 states that monthly bank reconciliations should be prepared within 30 days of the bank statement date, and reviewed by management for appropriateness and accuracy. Hudson did not prepare its monthly bank reconciliations within 30 days and the reconciliations were not always signed and dated by the preparer and reviewer.

**Recommendation**

21. If DCFS considers contracting with Hudson in the future, Hudson management prepare monthly bank reconciliations within 30 days from the bank statement date and ensure that the reconciliations are signed and dated by both the preparer and the reviewer.